SUPREME COURT, U. S.

MAY 21 1969

JOHN F. DAVIS, CLERK

IN THE

Supreme Court of the United States

October Term, 1968.

No. 1369.

In the Matter of

COMMONWEALTH FINANCIAL CORPORATION AND ITS SUBSIDIARIES, NEIGHBORHOOD FINANCE CO., INC. AND NEIGHBORHOOD FINANCE CO., INC. OF PENNSYLVANIA, Debtors.

MORISE THAL, Petitioner.

On Petition for Writ of Certiorari to the United States Court of Appeals for the Third Circuit.

BRIEF IN OPPOSITION FOR RESPONDENTS RALPH W. PITMAN AND ISADORE H. BELLIS, TRUSTEES.

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INDEX.

	Page
QUESTIONS PRESENTED	1
STATEMENT OF THE CASE	2
ARGUMENT	3
I. The Decision in This Proceeding by the Court of Appeals Is Not in Conflict With Other Reported Cases	3
II. The Instant Case Is Not the First Decision Authorizing the Commission to Examine Witnesses in Chapter X Proceedings	5
III. The Instant Decision Is Clearly Correct and Is Not in Derogation of the Legitimate Rights of Petitioner	6
CONCLUSION	11

TABLE OF CITATIONS.

Cases:

	Page
Communist Party v. Subversive Activities Control Board, 367 U. S. 1 (1961)	9
In re Hoffman Can Corp., 373 F. 2d 622 (CCA 3rd, 1967)	9
Securities and Exchange Commission v. Krentzman, 397 F. 2d 55 (5th Cir. 1968)	5
Securities and Exchange Commission v. Templar, 405 F. 2d 126 (CCA 10th, 1969)	3, 4
United States v. Simon, 373 F. 2d 649 (CCA 2nd, 1967), certiorari granted sub nom., Simon v. Wharton, 386 U. S. 1030 vacated as moot, 389 U. S. 425 (1967)	9

Statute:

Bankruptcy Act:

Section 167 (11 U. S. C. A., Sec. 567)	3, 4, 5, 6, 7, 8, 9, 10, 11
Section 169	5
Section 179	5
Section 208 (11 U. S. C. A., Sec. 608)	3, 6

U. S. Constitution:

Fifth Amendment	9

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COMMONWEALTH FINANCIAL CORPORATION AND ITS SUBSIDIARIES, NEIGHBORHOOD FINANCE CO., INC. AND NEIGHBORHOOD FINANCE CO., INC. OF PENNSYLVANIA, *Debtors.*

MORISE THAL, *Petitioner.*

ON PETITION FOR A WRIT OF CERTIORARI TO THE UNITED STATES COURT OF APPEALS FOR THE THIRD CIRCUIT.

BRIEF IN OPPOSITION FOR RESPONDENTS RALPH W. PITMAN AND ISADORE H. BELLIS, TRUSTEES.

QUESTIONS PRESENTED.

Respondents have no objection to the statement of Questions No. 1, 2 and 3(a). Respondents object to Questions 3(b) and (c) as containing factual matter not suported by the Record. (See Statement of Case below.)

STATEMENT OF THE CASE.

The facts as set forth in Petitioner's statement are correct except as hereafter supplemented or modified.

Petitioner is the chief executive officer of the Debtor, and his testimony is essential to a full understanding of the complex operation of Debtor's business and past transactions, involving 12 subsidiary corporations and over 9 million dollars in assets.

At the inception of the depositions, counsel for the Securities and Exchange Commission did not indicate an intention to direct his interrogation to violations of the Securities Acts. Because the contemplated examination of the witness (Petitioner) with respect to the legitimate subject matter of the reorganization proceeding might disclose facts which tend to show criminal violations, the witness was properly cautioned that this might occur and that his privilege against self-incrimination was available, should he desire to exercise it.

At no time has the Commission or counsel for the Trustees conceded that the Commission has disclosed or will disclose to the Trustees information developed in its non-public investigation. The disclosure of such information, if it should take place, is deemed to be irrelevant to the issues in this appeal.

Although the following information is not formally a part of this record, the Court of Appeals was advised at the oral argument by counsel for Respondents, and it is a matter of public knowledge, that Petitioner was indicted in December 1968 by the Commonwealth of Pennsylvania on various charges of embezzlement, making fraudulent acts and falsifying corporate records, as to transactions involving the Debtor in December 1962.

ARGUMENT.

I. The Decision in This Proceeding by the Court of Appeals Is Not in Conflict With Other Reported Cases.

Section 208 (11 U. S. C. A., Sec. 608) of the Bankruptcy Act permits the Securities and Exchange Commission to intervene and become a party to a corporate reorganization proceeding under Chapter X. It provides, in part:

> . . . "the Commission shall be deemed to be a party in interest, with the right to be heard on all matters arising in such proceeding . . ."

The Commission became a party and has participated in these proceedings. Subsequently, the Trustees were authorized to conduct an examination of witnesses, including Petitioner as an officer of the Debtor, pursuant to Section 167 (11 U. S. C. A., Sec. 567). By further order, the court authorized the Commission to participate in such examination.

Petitioner refused to be sworn or to testify on the ground that the Commission had no right to participate.

The Court of Appeals, in affirming the judgment of the District Court, held that the Commission has the right to participate in an examination of witnesses under Section 167. The authority for such participation is derived from Section 208.

Petitioner refers to *Securities and Exchange Commission v. Templar,* 405 F. 2d 126 (CCA 10th, 1969) as creating a conflict between the circuits, at least in principle. The cited decision is readily distinguishable from the instant case. In *Templar,* the Trustee amended his plan of reorganization by omitting a provision classifying stockholders as creditors, the earlier provision having been based upon

certain alleged misrepresentations by the Debtor. No stockholder filed a claim within the time fixed by the court or took any other action. Thereafter, the Commission presented a motion to have the omitted provision reinstated. The Court of Appeals held that the Commission, under the circumstances, had no standing to press the motion on behalf of stockholders, who were now barred from filing claims. The Commission, the court stated, could not assert "superior rights" to those of the shareholders.

Petitioner argues that in the instant case (contrary to the spirit of the *Templar* holding) the court accorded the Commission a "superior" right to examine witnesses which, it is claimed, is not available to individual holders of securities.

The analogy is unsound.

In *Templar,* the Commission was attempting to secure for stockholders substantive rights which individually they were barred from presenting. Certainly it was not unreasonable for the court to refuse to allow the Commission a "superior" standing than the shareholders had in the protection of their individual rights.

In the present situation, the plan is still to be filed, and no time has been fixed for the filing of claims by the holders of securities. The rights of security holders have not yet been adjudicated. Section 167 provides that the Trustee shall make an investigation of the financial affairs of the Debtor if the court so authorizes. It does not provide that *only* the Trustee may participate in the investigation. The objective of the examination is to develop information which will benefit creditors and shareholders. However, it is not practical to allow every member of a large group of creditors or shareholders to participate individually in the examination of witnesses. This function is performed by their representatives, namely, the Trustee, creditor and share-

holder committees, and the Securities and Exchange Commission. The rights exercised by their representatives in examining witnesses are those, in effect, belonging to the creditors and shareholders, on whose behalf and for whose benefit the investigation is conducted. Accordingly, the Commission is not invested with standing "superior" to that of creditors and shareholders but rather is the means, with the Trustee and committees, of implementing, in the only practical way, those rights fundamentally belonging to creditors and shareholders.

In an appropriate case, in the discretion of the court, an individual creditor or shareholder might well be permitted to participate in the examination of a witness. This occurs more logically from time to time in the hearings under Sections 169 and 179, respectively, on the approval and confirmation of the plan. But, there is no reason why it cannot be done in the 167 investigation as well.

II. The Instant Case Is Not the First Decision Authorizing the Commission to Examine Witnesses in Chapter X Proceedings.

In *Securities and Exchange Commission v. Krentzman*, 397 F. 2d 55 (5th Cir. 1968), the court held that the Commission had the right to participate in a hearing on a petition by a Chapter X Trustee to recover property, consisting of a block of stock, from a third party, and *such participation included the right to cross-examine witnesses.* The court stated that to deny the Commission the privilege to examine witnesses constituted an abuse of discretion. Although the cited case was directly concerned only with the interrogation of witnesses in a specific controversy between the Trustee and third parties, the opinion of the court was based upon the board principle that the Commission's participation in a reorganization proceeding is

almost unlimited in scope. It will certainly be difficult, if not impossible, for the Commission to discharge its many responsibilities under Chapter X of the Bankruptcy Act unless it can join in all examinations of witnesses whether by way of discovery or in connection with specific disputes. Actually the right of the Commission to question witnesses would appear to be much more logical and important in discovery proceedings if it is to do its job effectively than in regard to a hearing involving a specific controversy with a third party. Accordingly, the recognition of such right in the latter instance would a fortiori embrace the former.

III. The Instant Decision Is Clearly Correct and Is Not in Derogation of the Legitimate Rights of Petitioner.

Section 208 of the Act (quoted above) is a broad grant of status and authority, establishing clearly that the Commission is a party for all purposes and has the full right to be heard on all matters.

Petitioner appears to agree that the Commission, as a disinterested and expert agency, has extensive powers and duties in a reorganization proceeding, in the nature of an *amicus curiae*. Petitioner argues, however, that the Commission's authority is limited and is mainly advisory, that Section 208 does not include the right to examine witnesses in a Section 167 examination, and that such examination is restricted to the Trustees. Section 167 provides that the Trustee shall make an investigation of the financial affairs of the Debtor if the court so authorizes. It does not provide that *only* the Trustee may participate in such investigation. Even though individual creditors and shareholders may be excluded from taking part in 167 examinations, in the discretion of the court, by reason of the practical difficulties and additional burdens their widespread participation might impose, certainly creditor and share-

holder committees and the Securities and Exchange Commission fall into a different category. As a party to the proceedings entitled to be heard on all matters, the Commission could not effectively perform its functions under the Bankruptcy Act without the right to examine witnesses. The role of the Commission is not merely as an advisor of the Trustee. It is also an independent agency charged with the protection of the public before the court; and it must be assumed that Congress in granting the Commission the right to be heard on all matters intended that it be empowered by all usual means, including the right to examine witnesses, to carry out this responsibility in the fullest sense.

Petitioner contends that even if the Commission generally has the right to participate in an examination by a Trustee under Section 167, this right should be denied in this case because the Commission is presently conducting a non-public investigation of the Debtor and of Petitioner as an officer of the Debtor to ascertain whether criminal violations of federal securities laws have been committed.

Petitioner fails to explain satisfactorily how the concurrence of the two investigations, one by the Commission and the other by the Trustees, provides a legal premise for objecting to the latter. He appears to be arguing that he fears the Commission will, in the Trustees' examination, have the benefit of a second attempt to develop criminal violations. But, the two investigations have different objectives. The Commission is seeking to establish violations of the securities laws. The Trustees are trying to develop facts concerning the assets, liabilities, acts, conduct and financial transactions of the Debtor. The Trustees require such information to assist them in formulating a plan of reorganization and also to determine whether any wrongdoing occurred which would give rise to causes of

action for damages or the recovery of property. The Commission's participation in a Chapter X proceeding is restricted to the inherent purposes of such proceeding. As a by-product, the Chapter X examination may develop material relevant to the reorganization which also tends to show the existence of criminal offenses. This occurs frequently in bankruptcy proceedings but is hardly a justification for staying an investigation as long as witnesses are accorded their full constitutional privileges.

Realistically, all that Petitioner seeks to accomplish is the avoidance of the necessity of exercising his privilege against self-incrimination. The apparent purpose of this appeal is to delay such occasion. As a witness, he is fully protected by his right to assert his constitutional privilege against self-incrimination during any examination which may be conducted by the Trustees or the Commission.

An indefinite stay of his examination would defeat the clear objectives of two coordinate Acts of Congress. The Securities Acts of 1933 and of 1934 authorize the investigation and the private examination now being conducted by the Securities and Exchange Commission. Section 167 of the Bankruptcy Act provides for the examination presently being sought by the Trustees. The fact that the two examinations may overlap and that representatives of the Commission are parties to the reorganization proceeding creates no special prejudice or legal burden for the witness which is not justified by the overall situation and the necessity to complete the tasks at hand. The coincidental interaction of the operation of the two Congressional enactments is entirely consistent with their respective provisions, and in no way represents a conflict of policy.

The witness is not entitled to a blanket invocation of the privilege against self-incrimination. Nor may he have

general protection from possibly incriminating questions other than by asserting his constitutional rights under the Fifth Amendment. *Communist Party v. Subversive Activities Control Board,* 367 U. S. 1, 108 (1961); *In re Hoffman Can Corp.,* 373 F. 2d 622 (CCA 3rd, 1967).

United States v. Simon, 373 F. 2d 649 (CCA 2nd, 1967), *certiorari granted sub nom., Simon v. Wharton,* 386 U. S. 1030 *vacated as moot,* 389 U. S. 425 (1967), is not directly in point. There the Trustee in a Chapter X reorganization proceeding sued to recover damages resulting from a conspiracy to despoil assets of the Debtor. In the pending civil action, the Trustee sought to take the depositions of the defendants. A motion to stay the depositions was filed on the ground that a criminal prosecution was pending against the same defendants based upon facts substantially similar to those set forth in the civil complaints. The protective order was denied.

The present appeal involves a general examination of a witness as part of the overall reorganization proceeding. No civil action has been instituted against him although he has been indicted by the State authorities.

Petitioner further contends that the participation of the Commission in the Trustees' examination, which is, of course, public, in effect enables the Commission to conduct both a private and public investigation at the same time without according the witness the same rights and safeguards available to him under Securities Regulations. As pointed out above, the examination by the Trustees is pursuant to the provisions of Section 167 of the Bankruptcy Act and has entirely different objectives from the private investigation of the Commission. The attorneys for the Commission are taking part in the reorganization proceeding within the scope of its purposes and will be bound thereby in their examination. Questions, if any, designed

solely to establish criminal violations and having no bearing on the subject matter of the reorganization proceeding as defined in Section 167 will be objectionable.

Petitioner argues that the Commission has already indicated an intention to violate the permissible scope of the examination under Section 167 as demonstrated by the warning of its attorneys to the Petitioner at the inception of the depositions that he is entitled to refuse to answer questions on the ground of self-incrimination inasmuch as violations of the securities laws may be involved in his testimony. Petitioner distorts the purport of the Commission's statement to the witness. It in no way supports the assertion that the Commission plans to ask questions conceived primarily to show criminal offenses under the federal securities statutes. As set forth above, interrogation directed to the legitimate objectives of the reorganization proceeding may well disclose facts which tend to show criminal violations. The Commission's statement quite properly cautioned the witness that this might occur and suggested to him that his privilege against self-incrimination will in such event be available should he desire to exercise it.

Finally, Petitioner complains that the Commission, in violation of its own Rules, has expressly or unconsciously given the Trustees information developed in its non-public investigation, or the benefit thereof. If it be true that in consultations between counsel for the Trustees and representatives of the Commission assistance has been unwittingly given stemming from material developed in the non-public investigation of the Commission, this can be counted as a coincidental by-product inherent in the Congressional scheme of two concurrent and overlapping procedures under separate statutes designed to effectuate different but related policies. It is to be noted that the secrecy

Rule applying to the results of the Commission's non-public investigation originated with the Commission, not with Congress, and disclosure may be made if authorized by the Commission. In any event, a violation of the Commission's Rule without a showing of complicity on the part of the Trustees is a matter between Petitioner and the Commission. It represents no proper ground for staying the examination of the Trustees under Section 167.

CONCLUSION.

For the foregoing reasons, it is respectfully submitted that this petition for a writ of certiorari should be denied.

Respectfully submitted,

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MAY 14, 1969.